

**SALES AND USE TAX REVIEW COMMISSION
RECOMMENDATION PURSUANT TO P.L. 1999, C. 416**

BILL NUMBER:

A-1460

DATE OF INTRODUCTION:

January 10, 2006

SPONSOR:

Assemblyman Conners
Assemblyman Conaway, Jr.
Assemblyman Voss

DATE OF RECOMMENDATION:

February 7, 2006

IDENTICAL BILL:

A-4181, S-2805

COMMITTEE:

Assembly Education Committee

DESCRIPTION:

The bill exempts certain purchases by school food service providers from the sales and use tax.

ANALYSIS:

This bill provides for an exemption from sales and use tax of supplies, materials and equipment purchased by school food service providers used directly and exclusively in operating a food service in a public, nonpublic or charter school pursuant to a contract with a board of education, board of trustees or person having responsibility for the operator of the school in this State.

Generally, New Jersey schools are exempt from sales and use tax on purchases made with school funds under N.J.S.A. 54:32B-9. This bill seeks to create an exemption based on a taxpayer's contractual relationship to an exempt entity.

The Commission recommends that in lieu of providing a specific exemption for school food service providers, N.J.S.A. 54:32B-9 be amended to specifically deal with agency relationships between contractors and an exempt entity. The existence of an agent/principal relationship determines whether the purported agent may utilize the sales tax status of the principal. Specifically, the following factors should be considered in determining whether an agency relationship exists between the parties:

- Title to goods and liability for loss pass immediately to the principal at the point of purchase made by the agent. The principal insures and/or indemnifies the agent's transactions made on its behalf.
- The agent exercises no ownership rights over the property purchased on behalf of the principal.
- Disclosure of the principal/agent relationship is made to vendors with whom the agent is making purchases as purchasing agent for the principal. The vendor must

bill or invoice the purchase to the principal or to the contractor, specifying that the contractor is acting as an agent for the principal. The bill or invoice must identify the place of delivery. Deliveries must be made to the site specified in the contract with the principal or if to another site, the bill or invoice must identify where the items will ultimately be delivered under the terms of the contract with the principal.

- Payment must be made by the principal or to the contractor directly to the vendor from a special fund created by the principal for the purchases.

The following is also taken into consideration:

- The agent's activity that is subject to the principal's right to approval or control (e.g. manner of conducting business where principal actually exercises control or supervision).
- Agreement/contract language used designates the parties with "principal/agent" language.

The above factors are not exhaustive and other facts may also be examined. No factor above is independently determining.

The bill as written benefits a specialized group and does not promote horizontal equity. Horizontal equity mandates that sales tax legislation be broadly based and taxes similar transactions, persons or things in a similar manner. Tax treatment should be uniform from one taxpayer to another. This proposal creates a disparity between school food service providers and taxpayers in other professions not qualifying for the exemption. If this bill is passed as written, it could open the door to allowing other agents an exemption as well. For instance, agents to federal contractors, colleges, universities, and prisons will also claim an exemption due to horizontal equity. If the State does not allow such an extension, these parties may bring a lawsuit against the State of New Jersey for discrimination which could cost the State millions of dollars.

The Commission also suggests that school food service providers structure their relationships with Boards of Education in order to establish a true agency relationship.

The bill's broad language leads itself to many administrative and enforcement problems. The bill does not define "supplies, material and equipment" or "food service management provider." This language allows for subjective interpretation and may result in fraudulent purchases. Enforcement and administrative problems arise because of the inherent difficulty in determining whether a purchaser and the purchase are qualified for the exemption. Finally, the food service provider who purchases equipment and has among other business obligations, a contract which provides for eligibility might within the language of the law be required to own duplicate equipment for service not provided under such a contract.

According to the legislation, the act shall take effect immediately and shall be retroactive to July 1, 1999. This will have the result of ending any pending assessments. However,

it is not clear how past assessments should be handled. Pursuant to N.J.S.A. 54:32B-20, if application is made within four years from the date of the payment of the tax, the Division is required to issue a refund of tax paid in error, illegally or unconstitutionally. Thus, if the intent of the legislature is to have the Division issue refunds, this statute must be amended to permit refunds of tax remitted on and after July, 1, 1999.

Since there was no taxpayer reliance on unsettled law and the money is not to be refunded to the municipality, the bill should include a provision prescribing a window such as 30 days, in which application for refund should be made. This provision is necessary in order to restore certainty to public finances and to mitigate a potential windfall from being returned to the vendors who are engaged in food service contracts with municipalities.

The Commission does not recommend enactment of this bill.

COMMISSION MEMBERS FOR PROPOSAL: 1

COMMISSION MEMBERS AGAINST PROPOSAL: 8

COMMISSION MEMBERS ABSTAINING: 0

The Commission recommends that comments be added to this recommendation. A Motion to Clarify Legislative Intent was passed which stated: The Commission would support legislation that would clarify the rules for agency under Section 9 of the Sales and Use Tax Act and eliminate the retroactivity clause as proposed. The Commission agrees with the overall intent that there should be no adverse tax consequences to a food service business purchasing supplies solely for use in fulfilling a contract with a primary or secondary a school.

COMMISSION MEMBERS FOR MOTION: 9

COMMISSION MEMBERS AGAINST MOTION: 0

COMMISSION MEMBERS ABSTAINING: 0

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